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BILATERAL DIALOGS

13. (SBU) Tokyo Sub Cabinet Meetings

A six-agency Sub Cabinet team, led by Deputy National Security Advisor for Economic Affairs Dan Price met December 6-7 with their Japanese counterparts, headed by Deputy Foreign Minister Masaharu Kohno.

The meetings covered a range of bilateral, regional and global issues, including climate change, Doha, development assistance, U.S. beef exports, and medical devices and pharmaceuticals. In conjunction with the visit, Price delivered a speech on U.S.--Japan economic relations at a function co-sponsored by the Japan Association of Corporate Executives (Keizai Doyukai) and the American Chamber of Commerce in Japan. (Econ: Nicholas Hill)

14. (SBU) Megaports Discussions Continue

The GOJ continues to cogitate about Megaports, with comments to USG officials in the Sub Cabinet and Regulatory Reform dialogues indicating Japanese commitment to the program. See Tokyo 5478 for details on the Megaports experts meeting Nov. 28--30. (ECON: Charlotte Crouch)
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15. (SBU) Chuokeiren Vice Chairman Frustrated With China; Favors FTA

Akira Yokoi, Vice Chairman of the Chuokeiren and former Chairman of Toyota Industries, was very critical of China at a December 4 meeting in Nagoya with visiting DAUSTR for Japan Michael Beeman. Yokoi said that, while taking easier steps like

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lowering tariffs, China has ignored major commitments associated with its accession to the WTO including national treatment for foreign automakers and IPR obligations. The PRC's refusal to allow more than 50 percent ownership for foreign firms in the auto sector has hampered Toyota's efforts to fully introduce the Toyota Production System in China, he said. Yokoi acknowledged that dealing with China is extremely sensitive but said it would be a big mistake if Japan "keeps quiet."

Yokoi said that, without a bilateral U.S.-Japan FTA, Japan's economic future would be dim, particularly in light of the growing web of intra-Asia trade agreements that threatens to shut out Japan. Although Japanese automakers are wary of coming out too strongly in favor of an FTA that includes agriculture, Yokoi said, he understands the necessity of including all sectors and hopes there is enough political will in Tokyo to make it so. (Nagoya: Tamiki Mizuno)
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16. (SBU) Japan-China High-level Econ Dialogue Yields Minimal Results

The first session of the Japan-China High-level Economic Dialogue (HED), Japan's version of the U.S.-China Strategic Economic Dialogue, produced little in the way of tangible results. Held December 1 in Beijing, the meeting, attended by six Japanese Cabinet ministers, reviewed a number of areas for stronger cooperation between the two countries but without specifying any real activities. A MOFA official who attended the talks noted Chinese approval of the Japanese Environment Ministry's "co-benefit approach" on pollution and global warming and the intention to establish an information sharing system on intellectual property violations in China as two of the HED's most substantive achievements. The official also indicated the Japanese did not assent to China's request to be recognized as full market economy in the WTO. A separate December 1 meeting between the Chinese and Japanese foreign ministers achieved no progress on the East China Sea dispute except to stress that both countries hoped to resolve the issue in the near future before Prime Minister Fukuda's expected trip

to China (as yet unscheduled). (ECON: Chris Wurzel)

HEALTH ISSUES

17. (SBU) Embassy Concerned About Looming Changes to GOJ
MedPharm Pricing Policies

The Embassy has raised concerns with the GOJ about the government's reimbursement pricing for medical devices and pharmaceuticals. Final decisions on price levels for drugs and devices under the framework will be made in the coming days and is set to be announced on December 12.

To encourage innovation in what is a rapidly growing sector, the United States has pushed for policies that create a fair and predictable reimbursement environment. Some U.S. companies have complained that Japan's reimbursement policies are leading them not to introduce some of their best products into Japan.

In particular the United States objects to a drug re-pricing policy based on market expansion--that is, a scheme under which the GOJ slashes the price it pays for some drugs when producers enjoy larger than expected growth in sales. The policy penalizes the most widely recognized and innovative medicines for their success in treating disease.

For medical devices, the U.S. has concerns about a foreign average price rule which caps reimbursement prices at 1.5 times the average price in the United States, Britain, France, and Germany for devices already on the market and two times the average for new devices. The GOJ wants to slash the latter cap from 2.0 times to 1.7 times.

The Ambassador met with Health Minister Yoichi Masuzoe on December 5 to underscore U.S. concerns. For more on that meeting, please see Tokyo 5471. (Econ: Nicholas Hill)

FARMING AND AGRICULTURE

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18. (U) Furious Fukuoka Farmers Demand Subsidy Revival

Calling for the revision of the government's farm subsidy system that caters only to large farms producing major staples such as rice and wheat, 3,700 local farmers converged on central Fukuoka on December 1. A number of Fukuoka LDP Diet members, including Makoto Koga, Election Strategy Chief, attended the pre-demonstration rally in an effort to limit political fallout. The demonstration was the largest so far by Fukuoka farmers.

The demonstrators criticized the subsidy system (introduced in 2007), claiming it has not been successful in assisting the large farms it was supposed to protect. Instead, they insist, it has led to a decline in farm incomes despite a good harvest year. An estimated seven percent of small scale Fukuoka dairy farmers (183 households) have been forced out of business over the past year as a result of the rise in oil and feed prices. The farmers demanded redress against falling rice prices and the protection of Japanese agriculture in future free trade agreements.

Note: Responding to pressure with an election on the horizon, the LDP recently announced plans to review its farm subsidy system, possibly revising it to include small scale farms in the fiscal 2007 supplementary budget. Moreover, in a meeting with Fukuoka Prefectural Assembly leaders from the LDP, farmers explained the LDP was actively courting small farmers to bring them back to the LDP fold. They claimed the defection to the DPJ by farmers in the recent Upper House election was a temporary reaction to the Koizumi reforms, but now that the LDP

was addressing the farmers' concerns the defections could be reversed and the LDP's hold on the prefecture would be consolidated. (Fukuoka: Yuko Nagatomo/James Crow and Takafumi Sato/Margot Carrington)

9. (U) Hokkaido Governor to Ask Local Legislature to Continue BSE Testing

Late last week, local newspapers headlined Hokkaido Governor Harumi Takahashi's decision to request funding from the Hokkaido Prefectural Assembly to pay for continued BSE testing on cattle 20 months and younger. She will ask the assembly to approve an additional 70 million Yen (\$636,000) to cover the cost of testing 77,000 cattle 20 months and younger once the GOJ cuts off funding in July 2008. Local analysts already predict a 50 billion Yen (\$455 million) deficit in Hokkaido's budget next year; it is not clear where the money will come from.

Unlike other beef producing prefectures in Japan, Governor Takahashi did not immediately call for local funding of BSE testing when the GOJ announced it would no longer fund the tests. Instead, the governor made several trips to Tokyo to appeal directly to the Ministry of Agriculture, Fisheries and Forestry and the Ministry of Health, Labor and Welfare for reconsideration. With no success -- and other prefectures such as Miyazaki and Niigata stating they will fund continued testing -- the governor now feels compelled to do the same. Despite no proven scientific value to conducting BSE testing on all cattle, local Hokkaido residents seem to agree. A Hokkaido Prefectural Government survey and discussions at recent public hearings show over 70 percent of local consumers support continued BSE testing. Local farmers also fear that without the tests, Hokkaido's beef will be perceived as unsafe. Hokkaido is Japan's top beef producer. A total of 22 of Japan's 33 confirmed BSE cases were found in Hokkaido. A series of recent food scandals originating in Hokkaido has further shaken consumer confidence in local products. (Sapporo: Ian Hillman/Yumi Baba)

10. (U) Shiga Exports Beef to U.S.

JA Shiga Headquarters has started to export "Ohmi Beef," Shiga Prefecture's well-known brand of beef, to the U.S. in a pilot project. JA is targeting high-end American restaurants with a taste for prime Japanese beef. Exports in the pilot total one ton of sirloin, rib, and another four cuts, destined for Los Angeles.

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The demand for Japanese beef in large cities such as New York and Los Angeles has increased after the exports from Japan resumed in 2005. So far, Japan has exported 54 tons of its expensive beef since the resumption of trade. JA Shiga expects to enhance the motivation of local livestock farmers and expand the market in the future. (Osaka-Kobe: Phil Cummings/Naomi Shibui)

MONEY MATTERS

11. (SBU) ConGen Econ Officer Promotes Investment and Economic Revitalization in Nara

Osaka-Kobe Pol-Econ Officer spoke to 50 representatives of local political, business, media and Buddhist leaders on ways to revitalize the economy of Nara Prefecture at the Nara Chamber of Commerce and Industry this week. Nara has begun to strengthen its business promotion strategy, a hallmark of new Governor Shogo Arai. Both Nara City and the prefecture have pushed new tourist promotion campaigns, including plans to attract luxury American hotels to Nara. The mayor already announced that it will bring a Marriott to open in the city center in a couple of years. This stole the thunder from Gov.

Arai, who had been working with ACCJ and METI Kinki Bureau to bring a different American hotel to the city, underlining continuing problems in convincing the different levels of bureaucracy to work together on economic development. Nara is gearing up to the 2010 1300th anniversary of the establishment of Heijo-kyo, the ancient 8th Century Japanese capital predating Kyoto.

Pol-Econ Officer pointed out problems with the poor tourist infrastructure in Nara, the small levels of FDI, and lack of cooperation among local governments and businesses, despite the abundance of tourism resources in Nara. The reaction of local audience was very receptive to these messages, and Nara Prefectural officials commented that they will make use of these suggestions in improving their economic planning and coordination. (Osaka-Kobe: Phil Cummings/Naomi Shibui)

112. (SBU) Tourism--Kyoto Popular Among Americans, but No Growth

MLIT Kinki Transportation Bureau recently released the study of tourist trends in the Kansai for the first half of 2007. It showed that 13.6 percent of tourists in Japan visited the Kansai's six prefectures, and 80 percent of those visitors stay in three prefectures: Osaka, Kyoto, and Hyogo. The largest number of the Kansai's foreign tourists is from South Korea, followed by Taiwan. Tourists from the U.S. came in third. Amid the trend of rapid growth in Asian tourists visiting the region, American tourists still make up over a quarter (26 percent) of the total foreigners who stay overnight in Kyoto, the largest group.

This survey is the Kinki Transportation Bureau's first attempt to analyze lodging tourists rather than day travelers. One official told ConGen that the Kansai has been successful in attracting Asian tourists, but attempts to lure American and European travelers remain problematic, since the GOJ's Western-oriented tourism promotion is still in its infancy. American travelers love Kyoto, but their numbers are flat, according to the official. (Osaka-Kobe: Phil Cummings/Naomi Shibui)
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113. (U) Restrictive City Planning Law for Large Retail Stores Went into Effect November 30

The amended Town Planning Law went into effect on November 30. The law is expected to restrict new establishment of large retail stores and shopping malls in the suburbs, and it is aimed at revitalizing city centers by restricting the opening of commercial facilities with total floor spaces of more than 10,000 sq. meters.

According to Mainichi Shinbun, some retailers have already started coordinating with local governments over the opening of new stores, foreseeing the amendment of the law. Retail industry is promoting a campaign to have the openings of large stores incorporated into local governments' development plans.

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(ECON: Junko Nagahama)

114. (U) FY07 Supplemental Budget Won't Break the Bank

Press reports indicate that the FY07 supplemental budget being compiled by the Ministry of Finance will be limited to about Q1.5 trillion (\$14 billion). This is quite small by supplemental budget standards, and is a good indication that the GOJ is aiming to stick to its fiscal consolidation goals, despite some spending to address income and regional disparities. The supplemental will be finalized by MOF in mid-December, approved by the Cabinet in late December and submitted to the ordinary Diet session in January, 2008. Anticipated spending will cover disaster relief, Q150 billion to compensate for postponing the increase in medical payments by the elderly, additional aid for Afghanistan and UN programs, and possibly programs to support industries that have been hit

hard by the oil price spike. Finance Minister Nukaga told the press on December 5 that the government will not issue any additional bonds to pay for the supplemental, despite lower than expected tax revenues this fiscal year. (FINATT: Maureen Grewe)

115. (SBU) Kansai Manufacturers Face Hard Times; Bears Closing In

Most Kansai manufacturers have released closing accounts of the first half of JFY2007, April to September. According to the recent Nikkei Kansai Edition survey, although the average profit level of Kansai businesses increased eight percent from the previous year, profits are slowing annually, decelerating from 23 percent growth in 2005-6, and falling below the national average. Sharp, buoyed by LCD flat TV sales, dropped 12 percent in its profit margins nonetheless. In spite of increased sales, Matsushita (Panasonic) also fell back to 2006 nominal profits. Both companies blamed a drop in product demand in the U.S. market, the most competitive market for flat TVs, over the subprime loan problem and yen appreciation. Matsushita only reached 80 percent of its North American sales target.

Rising oil prices strongly affected the textile, chemical, and food industries, strong sectors in the Kansai. Most businesses in these industries shrank their profits over raising raw material costs. BOJ's Osaka Head Masahiro Samejima commented to the Sankei Shimbun Osaka edition that Kansai businesses depend on the world economy, so it might be hard to return to last year's high levels of growth until the global economy recovers. (Osaka-Kobe: Phil Cummings/Naomi Shibui)

116. (U) Minister Amari Concerned About Foreign Participation in JPower Management

Japanese media reported on November 4 The Children's Investment Fund (TCI), a UK investment fund known for its aggressive shareholder rights activities, has demanded JPower appoint two TCI executives to its board as outside directors. JPower, formally known as Electric Power Development Co., is the largest wholesale electric company in Japan. TCI is JPower's largest shareholder, holding 9.9% of the company's stock. JPower executives acknowledged receipt of a letter from TCI, but declined to publicly release its contents.

JPower was established as a state-owned company in 1952, but was privatized between 1997 and 2003, and listed on the Tokyo Stock Exchange in October 2004. At a November 4 press conference, Economy, Trade and Investment Minister Akira Amari stated he "cannot imagine" a foreign investment fund being involved in the management of such a highly important and sensitive infrastructure company so vital to Japan's national security. (ECON: (ECON: Eriko Marks)

AVIATION

117. (SBU) American Air Cargo Company Looks at Chitose in Hokkaido as Transport Hub

On December 1, a Hokkaido newspaper reported the Oregon-based air cargo company Evergreen is researching the possibility of developing a shipping route between the United States and China

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using Sapporo New Chitose International Airport. The proposed route would fly cargo from New York through Anchorage to Chitose. From Chitose, the airline would dispatch cargo to Shanghai and Hong Kong as well as other potential sites such as South Korea and Sakhalin, Russia. Evergreen Chairman Delford Smith reportedly plans to visit Sapporo in mid-December to ask Hokkaido Governor Harumi Takahashi for her support.

According to the article, Evergreen must overcome several

obstacles before the proposed shipping route can be realized. Challenges include obtaining GOJ approval to fly from Hokkaido to China, South Korea and Russia; establishing a cargo hub to station smaller aircraft at Chitose airport for region-based flights; and securing bonded facilities and warehouses around Chitose. In addition, conditions at Chitose airport itself must be improved to allow for late night flights and construction of a longer runway.

ConGen Sapporo has not yet been able to confirm that formal talks on a shipping route through Hokkaido are underway. However, prominent Sapporo businessman Yoshiro Ito, who was mentioned in the article, told Consul General Welton in October that he had met with Evergreen during a recent trip to the United States. Furthermore, Embassy Tokyo learned from MLIT International Aviation in November that Evergreen had asked Hokkaido airport authorities for permission to fly to China from Hokkaido. MLIT reportedly told Evergreen their request constitutes fifth freedom rights and would therefore have to be negotiated in government-to-government talks. Evergreen would not be the first American shipping company to propose utilizing Hokkaido as a gateway to China. In 2005, Federal Express tried to establish a similar route. That company's plans fell through after it was unable to obtain rights to fly from Chitose airport to other countries. (Sapporo: Ian Hillman/Yumi Baba)

OIL AND GAS

18. (SBU) GOJ Infighting Hampering East China Sea Talks

METI contacts told us that working-level negotiations regarding the dispute over East China Sea gas fields, which they previously called "a waste of time," have been positive over the last several months. However, higher level talks remain at an impasse, presumably due to political pressures in Tokyo to maintain a hard line with the Chinese. Please see Tokyo 5457 for more on this issue. (ECON: Sally Behrhorst/Eriko Marks)

19. (SBU) INPEX's Questionable Oil Deal

Japanese media report that INPEX Holdings, one of Japan's leading oil developers, will join forces with Canada's Ivanhoe Energy to explore for oil in the Qaiyarah oil field in Northern Iraq. According to a METI contact, INPEX hopes to capitalize on Ivanhoe's proprietary technology which simplifies the processing of Iraq's "asphalt-like" heavy crude. With total reserves estimated at 400-800 million barrels, daily production could reach 100,000 barrels if the venture is successful. Our contact told us, however, this deal is highly questionable given Ivanhoe's unproven technology claims and uncertain financial status. "They don't have a single processing plant to prove their technology works," he said. He demurred when asked to speculate why METI, which owns 30% of INPEX, would permit such an agreement. (ECON: Sally Behrhorst/Eriko Marks)

20. (U) GOJ to Offset High Cost of Crude Oil

Nearly 90% of small and medium enterprises (SMEs) have been adversely affected by the soaring cost of crude oil according to a November 29 report released by the Ministry of Economy, Trade and Industry (METI). In response, PM Fukuda on December 4 instructed his cabinet to find ways to assist SMEs and citizens most impacted by the high prices. Economic and Fiscal Policy Minister Hiroko Ota promised to study the issue and deliver recommendations the week of December 10. According to media reports, possible approaches include reducing highway tolls, easing loan repayment terms for SMEs and providing subsidies for heating oil to households in northern Japan. Chief Cabinet Secretary Nobutaka Machimura has suggested a portion of the supplemental budget may be used to fund this

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program. (ECON: Sally Behrhorst/Eriko Marks)

SPORTING NEWS

¶21. (U) Baseball's Greatest Team Set for Tokyo Dome,
Ambassador, Embassy Fans Will be There

The Boston Red Sox are coming to Tokyo along with the Oakland A's to open Major League Baseball's regular season on March 25 and 26. The Embassy has been offered the opportunity to purchase tickets and a group--including the Mission's chapter of Red Sox Nation--will be on hand.

The arrival of the Red Sox in Tokyo will be an historic opportunity to see baseball's greatest team. The Red Sox were Major League Baseball's first dynasty. They won the first World Series ever played in 1903 and a number of other championships since then, including the most recent World Series. The Red Sox include Japanese stars Daisuke Matsuzaka and Hideki Okajima.

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¶23. (U) This SENSITIVE BUT UNCLASSIFIED e-newsletter from U.S. Embassy Tokyo's Economic Section, with contributions from the consulates, is for internal USG use only. Please do not forward in whole or in part outside of the government. The Scope is edited this week by Charlotte Crouch (CrouchCA@state.gov) and Joy Progar (ProgarJ@state.gov). Please visit the Tokyo Econ Intranet webpage for back issues of the Scope. Apologies, this option is only available to State users. Please contact Joy Progar if you are from a different agency and are interested in a back issue.
SCHIEFFER